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No. 91-1421

IN THE

Supreme Court of the United States

OCTOBER TERM, 1992

UNITED STATES OF AMERICA,
Petitioner,

v.

WILLIAM F. HILL and LOLA E. HILL,
Respondents.

On Writ of Certiorari to the
United States Court of Appeals
for the Federal Circuit

BRIEF OF AMICI CURIAE THE NATIONAL COAL ASSOCIATION, CYPRUS MINERALS COMPANY, INDEPENDENCE MINING COMPANY INC., THE NORTH AMERICAN COAL CORPORATION, REDLAND INC., AND THE UNITED COMPANY IN SUPPORT OF RESPONDENTS

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STATEMENT OF INTEREST *

The National Coal Association is a non-profit trade association, with over 140 members, representing coal mining companies that own or operate more than 70 percent of the Nation's coal producing capacity. NCA producer

* Counsel for all parties have consented to the filing of this amicus brief. *Amici* have filed those consents with the Clerk of this Court.

members range from companies mining several thousand tons of coal yearly to large corporations producing millions of tons annually. NCA's members also include other key segments of the industry—coal sellers, equipment suppliers, resource developers, transporters, electric utilities, consultants and 32 state and regional associations. NCA is the principal spokesman for the United States coal industry.

The individual amici are engaged in the mineral extraction industry, and their tax liabilities are governed by the same minimum tax provision as the respondents in this case.

The result in this case, which involves oil and gas, will govern the hard minerals industry as well. Therefore, these amici or their members would suffer direct injury should petitioner succeed in establishing a new meaning of "adjusted basis of the property" for purposes of 26 U.S.C. § 57(a).

SUMMARY OF ARGUMENT

I.

This case involves the interpretation of a statute, 26 U.S.C. § 57(a)(8), which is part of the "minimum tax" provisions of the Internal Revenue Code. The minimum tax imposes a special levy on certain amounts that are excluded from the base of the income tax, as a result of various deductions or other benefits. Section 57(a)(8) subjects to the minimum tax a portion of a taxpayer's "percentage depletion" deductions, which the tax law provides in order to encourage mineral exploration and development.

Section 57(a)(8) provides that, for any taxable year, a taxpayer's percentage depletion deductions with respect to a mineral property shall be subject to the minimum tax *only* to the extent the deductions exceed the "adjusted basis of the property" at the end of the year. This case

involves the specific question whether the cost of depreciable tangible improvements to a mineral property, such as the pipes, pumps and other equipment necessary to operate respondents' property, shall be included in that property's "adjusted basis" for purposes of section 57(a)(8).

Congress enacted section 57(a)(8) against the background of a long history of interpretation under which the adjusted basis of a property, as defined under 26 U.S.C. § 1016, includes the cost of improvements to that property. Petitioner does not challenge this established understanding of "adjusted basis." Instead, petitioner urges that Congress should be assumed to have adopted a special definition appearing in a regulation under a provision of the Code not at issue here—a provision governing "cost," not "percentage," depletion. The special definition cited by petitioner by its terms applies *only* to cost depletion; moreover, the very need for that regulation, which provides a special meaning of "adjusted basis" for the limited purpose of the cost depletion rules, supports the view that the regular meaning of "adjusted basis" should apply in other areas. Against this background there is no ground for suggesting that Congress departed from the general definition of "adjusted basis."

II.

Even if 26 U.S.C. § 57(a)(8) were ambiguous, petitioner's own administrative interpretations make clear that the regular definition of "adjusted basis" is to apply.

This Court has "long recognized that considerable weight should be accorded to an executive department's construction of a statutory scheme that it is entrusted to administer . . . ." *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 844 (1984). Inherent in this rule is the principle that a government agency should not be permitted to disavow its own interpretations.

Petitioner's regulation, 26 C.F.R. § 1.57-1(h)(3)—the *only* regulation that directly addresses the meaning of "adjusted basis" for purposes of section 57(a)(8)—makes plain that the ordinary meaning of that term, as established at 26 U.S.C. § 1016 and in the regulations thereunder, should be applied. The regulations under section 1016, moreover, provide flatly that a property's basis is to be adjusted for the cost of improvements to the property. A 1982 technical advice memorandum issued by petitioner confirms this interpretation in the context of section 57(a)(8) itself.

Petitioner should not now be permitted, in the course of its appellate briefs, to substitute a new interpretation of the statute for the interpretation set forth in its own regulations. *Bowen v. Georgetown University Hospital*, 488 U.S. 204, 212 (1988).

ARGUMENT

I. THE PLAIN MEANING OF THE STATUTE CONTRADICTS THE GOVERNMENT'S INTERPRETATION.

This case involves two provisions of the Internal Revenue Code, 26 U.S.C. § 57(a)(8) and 26 U.S.C. § 1016(a), which are designed to operate in tandem.[1]

Section 57(a)(8) is part of the "minimum tax" provisions of the Code, which have existed in various forms since 1969.[2] The minimum tax is a superstructure placed on the general provisions of the Code. It was motivated by a congressional perception that various deductions and other tax benefits of the regular tax rules resulted, in some circumstances, in excessively low overall tax burdens for particular taxpayers. *See* H.R. No. 413, 91st Cong., 1st Sess. at 77-80 (1969). Thus, the minimum tax imposes a special levy on certain items that are excluded from the base of the regular income tax, as a result of various favorable deductions or other benefits that Congress has allowed in order to encourage particular kinds of economic activities. The regular tax benefits that the minimum tax to some extent "takes back" are commonly known as "preference items."[3]

Among the preference items that the minimum tax addresses is the "percentage depletion" allowance of 26 U.S.C. § 613 and related provisions of the Code. The Code provides two methods of calculating depletion. One method, "cost depletion," is in essence quite simple. If, for example, a taxpayer paid $1 million for an interest in a mineral property, and the mineral removed from the property in a particular year represents 10 percent of the estimated total mineral recoverable from the property, the taxpayer's annual deduction would be $100,000. Under cost depletion, once the cost of the deposit ($1 million in the example above) is fully recovered, no further depletion deductions are allowed.

[1] Unless otherwise specified, all citations will be to the Internal Revenue Code and the Treasury Regulations in effect in the tax years 1981 and 1982, the years at issue in this case.

[2] Pub. L. No. 91-172, § 301, 83 Stat. 581 (1969). Although the provisions of the minimum tax have been amended many times, the language of 26 U.S.C. § 57(a)(8) has remained unchanged since its original enactment. *See* Pub. L. No. 91-172, § 301, 83 Stat. at 582.

As a result of a restructuring of the minimum tax provisions in 1986, the language of section 57(a)(8), as it stood in the tax years at issue in this case, is now found at section 57(a)(1). Pub. L. No. 99-514, § 701, 100 Stat. 2330, 2333 (1986). This brief continues to refer to the provision as "section 57(a)(8)."

[3] For example, in the years at issue in this case, the minimum tax imposed a special levy on, among other items: (i) the excess of a taxpayer's "accelerated" depreciation on real property, over the amount that would be allowed under straight-line depreciation, 26 U.S.C. § 57(a)(2); (ii) the otherwise tax-deferred economic benefit received by an employee on receiving stock pursuant to certain employee stock options, 26 U.S.C. § 57(a)(6); (iii) the portion of a taxpayer's capital gain income otherwise shielded from tax, 26 U.S.C. § 57(a)(9); and (iv) the extent to which rapid amortization deductions allowed, under the regular tax rules, for child care facilities exceeded regularly allowable depreciation, 26 U.S.C. § 57(a)(10).

Percentage depletion is a more generous system, which was designed to encourage mineral exploration and production. As this Court noted in *Commissioner v. Engle*, 464 U.S. 206, 209 (1984), "[t]hrough these depletion provisions, Congress has permitted taxpayers to recover the investments they have made in mineral deposits and to generate additional capital for further exploration and production of the Nation's mineral resources." Under percentage depletion, the deduction allowed each year is *not* based, as a general matter, on the cost of the mineral in place. Instead, each year's percentage depletion is computed as a specified percentage of the gross income from the property for that year, subject to various limitations based on the net income realized from the property. 26 U.S.C. §§ 613, 613A. For example, in 1981 and 1982, the years involved in this case, independent oil and gas producers with relatively small volumes of production [4] were allowed percentage depletion at rates ranging from 18 to 22 percent of gross income, depending on the circumstances of production, and the deductions were not to exceed 50 percent of the net income from the property, or 65 percent of the taxpayer's overall taxable income. Despite the limitations placed on percentage depletion allowances, they often exceed the deductions that would be allowable under the cost depletion method. Moreover, because percentage depletion is not computed by reference to the cost of a property, percentage depletion deductions are not limited by that cost and can be taken, as a general matter, so long as production continues.

At particular issue in this case is the manner in which the minimum tax statute, at 26 U.S.C. § 57(a)(8), seeks to "take back" a portion of the percentage depletion allowance. Section 57(a)(8) provides that the items of tax

[4] Other oil and gas producers generally were allowed only cost depletion. Hard minerals producers, like small independent oil and gas producers, generally qualify for percentage depletion. 26 U.S.C. §§ 613-613A.

preference, for purposes of the minimum tax, shall include:

> [w]ith respect to each property (as defined in section 614), the excess of the deduction for depletion allowable under section 611 for the taxable year *over the adjusted basis of the property* at the end of the taxable year (determined without regard to the depletion deduction for the taxable year). (Emphasis supplied.)

The dispute between petitioner and respondent focuses on the meaning of "adjusted basis of the property," as used in section 57(a)(8).

The parties agree that determining the "adjusted basis of the property" requires reference to 26 U.S.C. § 1016. Section 1016(a) provides, in relevant part, that "[p]roper adjustment in respect of the property *shall in all cases be made . . . for expenditures . . . properly chargeable to capital account*." (Emphasis added.) Section 1016 thus makes clear that the costs of capital expenditures are added to the basis of the property. The original cost basis of the property is adjusted upward for the cost of improvements to the property. The statute governing adjustments to basis dates from the earliest days of the federal income tax,[5] and it provides straightforward support for the taxpayer's position.[6] The courts below properly held that, as defined and used in section 1016, "adjusted basis of the property" includes the unrecovered cost of improvements, both tangible and intangible, to the property. Thus, the courts below held that the adjusted basis of respondents' oil and gas properties should be adjusted for such im-

[5] The provision for adjustments to basis now found at 26 U.S.C. § 1016(a) was first enacted as part of § 202(b) of the Revenue Act of 1924, ch. 234, 43 Stat. 253, 255 (1924): "In computing the amount of gain or loss . . . proper adjustment shall be made for . . . any expenditure properly chargeable to capital account . . . ."

[6] As discussed below, the statute has long been interpreted by Treasury regulations that strongly support the taxpayer's position.

provements as the pipes, pumps and other machinery that have been placed on their properties in order to produce oil and gas.

The government seeks to avoid the result that necessarily flows from this longstanding and coherent approach. It notes that the introductory language in section 57(a)(8)—"with respect to each property (as defined in section 614)"—incorporates the definition of "property" appearing in section 614. (*See* Br. at 15).[7] Section 614, in turn, defines "property" to mean the "mineral deposit."[8] This is obviously correct as far as it goes. The difficulty is that section 57 does not define the preference item by the excess of depletion over the original cost basis of the property, *i.e.*, the original basis of the mineral deposit, but by the excess of depletion over the "adjusted basis" of the property. Both section 1016 and the regulations thereunder, which had long existed when section 57 was enacted,[9] require that basis be adjusted for "improvements" to the property. The government appears to admit, (*see* Br. at 23), that Congress must have legislated against this background. Accordingly, as the Federal Circuit held below, "absent a clear indication in the Code

[7] References throughout this amicus brief to "Br. at ——" are to the government's opening brief in this case.

[8] Br. at 15. The apparent purpose of section 614 is to provide a means for determining where one mineral property ends and another begins. This question can be important, because the calculation of depletion allowances, for purposes of both the regular tax and the minimum tax, depends in part on the extent to which properties are aggregated. *Cf.* 26 U.S.C. § 614(c) (giving taxpayer election whether to aggregate certain mineral properties for purposes of computing depletion); 26 C.F.R. § 1.57-1(h)(1) (1991):

> The determination under section 57(a)(8) is made with respect to each separate property. Thus, for example, if one mineral property has an adjusted basis remaining at the end of the taxable year, such basis may not be used to reduce the amount of an item of tax preference resulting from another mineral property.

[9] See discussion below, p.16-17.

or related regulations to the contrary," the established meaning of "adjusted basis" should apply. (Pet. App. at 11a.)

This Court's precedents make clear that when Congress employs a term that has a commonly understood meaning, it may be presumed to have incorporated that established construction into the statute. In *Cottage Savings Ass'n v. Commissioner*, 111 S.Ct. 1503 (1991), this Court held that in order for an exchange of property to constitute a "disposition of property" resulting in realization of taxable income under section 1001 of the Internal Revenue Code, 26 U.S.C. § 1001(a), the properties exchanged must be "materially different." The Court adopted this construction of the statute because the "contemporary legal context" at the time that Congress enacted section 1001 reflected a similar approach, and the Court presumed that Congress had intended to codify those principles in the statute. 111 S. Ct. at 1507-08.[10] So here Congress enacted section 57(a)(8) against a background in which there was a well understood interpretation of the term "adjusted basis of the property."

Unfazed by this logic, the government urges that the basis of the mineral deposit is not to be adjusted for improvements to the mineral property. (Br. at 21.) This argument is difficult to fathom. The government concedes that "the adjusted basis of a property generally includes 'the costs of improvements and betterments to a property' when these expenditures are 'properly chargeable to the [sic] capital account.'" (Br. at 21.) It also

[10] Similarly, in *Nationwide Mut. Ins. Co. v. Darden*, 112 S.Ct. 1344 (1992), this Court held that the term "employee," used in the Employee Retirement Income Security Act, carried its traditional common-law meaning. The Court wrote that "[w]here Congress uses terms that have accumulated settled meaning . . . a court must infer, unless the statute otherwise dictates, that Congress meant to incorporate the established meaning of those terms." 112 S.Ct. at 1348, *quoting Community for Creative Non-Violence v. Reid*, 490 U.S. 730, 739 (1989).

admits that "the machinery and equipment used in mineral production represent tangible 'improvements' to the mineral deposit." (Br. at 11; *see also* Br. at 23.) Indeed, the government goes so far as to agree that when the mineral property is sold, the adjusted basis for computing gain or loss must include these tangible improvements. (Br. at 24.)

However, the government claims that the regulations in effect before the minimum tax was enacted specifically provided an exception to the general rule—that for depletion purposes the mineral property and the improvements would be placed in separate capital accounts, so that the adjusted basis of the mineral property did not include the improvements.[11] (Br. at 21-23.)

The problem is that no such regulations existed. The regulations upon which the government relies are applicable only to cost-based depletion and not to percentage depletion. The government concedes that the regulation upon which it relies "pertains only to the basis for cost depletion" and that "[t]he regulations covering percentage depletion under Section 613 do not specifically address basis." While the government relegates these concessions to a footnote, (Br. at 18 n.13), in fact, these concessions are highly significant. Where there is no applicable regulation, it is quite impossible to conclude that Congress, without saying so, adopted the special cost

[11] The government's brief in support of this "separate account" theory misquotes the statute. Petitioner mistakenly quotes 26 U.S.C. § 1016(a) as providing for adjustments to basis for expenditures "properly chargeable to *the* capital account." (Br. at 21 (emphasis added).) In fact, section 1016(a)(1) refers to amounts "properly chargeable to capital account," without the "the" that petitioner has inadvertently inserted. Petitioner's slip is symptomatic of the fundamental misunderstanding of "adjusted basis of the property" that underlies petitioner's litigation posture in this case. "Adjusted basis of the property," as used throughout the tax laws, is an aggregate concept, as the Code makes clear. While one property may contain various cost recovery accounts, there remains one property, with one adjusted basis.

depletion rules for the percentage depletion calculations. Indeed, the very congressional directive that percentage depletion be limited to the "adjusted basis" of the mineral property necessarily assumed that the basis would be adjusted by the improvements to the property.

Petitioner's attempt to interpret a property's "adjusted basis" as excluding the cost of tangible improvements is inconsistent not only with the language of section 1016(a), but also with the language used in other provisions of the statute. Perhaps most important is the language of 26 U.S.C. § 611(a):

> *In the case of mines, oil and gas wells, other natural deposits*, and timber, there shall be allowed as a deduction in computing taxable income a reasonable allowance for depletion *and for depreciation of improvements*, according to the peculiar conditions in each case; such reasonable allowance in all cases to be made under regulations prescribed by the Secretary. (Emphasis added.)

Obviously this provision views depreciable improvements as components of the "mines, oil and gas wells, [and] other natural deposits" for which depletion is allowed.

Section 263(a)(1), 26 U.S.C. § 263(a)(1), one of the most central provisions of the Internal Revenue Code, indicates with similar plainness that "improvements" are part of the underlying "property." Section 263(a)(1) is designed to distinguish between those amounts, such as business expenses, that are deductible, and those amounts that are not deductible but instead must be charged to capital account. Section 263(a)(1) provides that deduction shall not be allowed for "[a]ny amount paid out for *new buildings or for permanent improvements or betterments made to increase the value of any property or estate*." (Emphasis added.)

There is simply no basis for reading the term "adjusted basis" in section 57(a) as having a special and unique meaning that would exclude improvements. When

a word or phrase is employed in different sections of a statute, it "is presumed to have the same meaning in all subsections of the same statute." *Patterson v. Shumate*, 112 S.Ct. 2242, 2447 n.2 (1992) (interpreting phrase "applicable bankruptcy law" so as to achieve uniformity of meaning within bankruptcy code).[12] Any other rule would be a recipe for confusion. Petitioner cannot, in the course of this litigation, insist upon a meaning of "adjusted basis of the property" for purposes of section 57(a)(8) that is different from its meaning in other provisions of the Internal Revenue Code.[13]

Alternatively, the government argues, in essence, that whether or not Congress said so, Congress must have intended to tax the excess of the depletion allowance over the basis of the mineral deposit (excluding improvements). In other words, if the property originally cost $1 million, and $2 million in improvements had been added, the tax preference should be in the amount by which depletion deductions exceeded $1 million rather than the amount it exceeded $3 million. This is fair, says the government, because depreciation attributable to the improvements is separately deductible. (Br. at 16-17.)

The difficulty with this argument is that it assumes rather than establishes the congressional purpose. The mere fact that Congress sought to impose a minimum tax and did not intend to permit a taxpayer to pay " 'a shockingly lower percentage of his income as tax,' " (Br. at 13), hardly establishes that Congress sought to impose the minimum tax on all the total amount of benefits from percentage depletion. Yet that is exactly what the government would do. If Congress had intended to do so, it would have been simple enough to craft the appropriate language. Congress did not, however, take this step.

Nor does the minimum tax as a whole reflect a congressional design to invariably impose a tax on all "unfair" benefits created by other sections of the Code, as the government suggests. (Br. at 28-29.) There is no inherent "logic" to that tax scheme. As one commentator has noted:

> Analysis of the alternative tax demonstrates that it is ill-conceived in every respect. The results reached by application of the alternative tax provisions are either inherently inequitable or involve unduly circuitous and cumbersome calculations.[14]

The essentially imprecise approach reflected in the minimum tax is perhaps best illustrated, for current purposes, by the preference for intangible drilling costs contained in the current version of the minimum tax. 26 U.S.C.

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[12] *See also Morrison-Knudsen Constr. Co. v. Director, Office of Workers' Compensation Programs*, 461 U.S. 624, 633 (1983) (term "wages" carries same meaning throughout Longshoremen's and Harbor Workers' Compensation Act); *Mohasco Corp. v. Silver*, 447 U.S. 807, 826 (1980) (rejecting interpretation of Civil Rights Act of 1964 that would give same word two different meanings).

[13] Petitioner looks in vain to the legislative history for significant guidance in this case. (*See* Br. at 25-26.) None of petitioner's references negates the view that "adjusted basis" includes improvements to the property. As the courts below noted in describing their own view of the legislative record:

> At oral argument, [the government] characterized the legislative history of Sections 56 and 57 as "not all that helpful." The court agrees. There are brief statements that arguably benefit each side, but nothing definitive.

(Pet. App. at 15a n.10.) Indeed, as the courts below noted, the conference report to the 1969 Tax Reform Act refers to the " 'cost *or other basis* on which the depletion preference is computed,' " language which suggests, in accordance with the plain language of the statute as enacted and in accordance with petitioner's administrative interpretations, that the basis referred to in section 57(a)(8) is the basis after adjustment pursuant to the regular rules for basis adjustment. *Id., quoting* H.R. Conf. Rep. No. 782, 91st Cong., 1st Sess. (1969), *reprinted in* 1969-3 C.B. 644, 659 (emphasis the courts').

[14] Glenn E. Coven, *The Alternative Minimum Tax: Proving Again That Two Wrongs Do Not Make A Right*, 68 Calif. L. Rev. 1093, 1094 (1980).

§ 57(a)(2) (1988 & Supp. 1992).[15] This provision shows plainly the attempt by Congress to achieve an essentially arbitrary balance between the interests of avoiding what was perceived as excessive use of favorable tax provisions,

[15] 26 U.S.C. § 57(a)(2) defines the preference as follows:

(2) Intangible drilling costs.—

(A) In general.—With respect to all oil, gas, and geothermal properties of the taxpayer, the amount (if any) by which the amount of the excess intangible drilling costs arising in the taxable year is greater than 65 percent of the net income of the taxpayer from oil, gas, and geothermal properties for the taxable year.

(B) Excess intangible drilling costs.— For purposes of subparagraph (A), the amount of the excess intangible drilling costs arising in the taxable year is the excess of—

(i) the intangible drilling and development costs paid or incurred in connection with oil, gas, and geothermal wells (other than costs incurred in drilling a nonproductive well) allowable under section 263(c) or 291(b) for the taxable year, over

(ii) the amount which would have been allowable for the taxable year if such costs had been capitalized and straight line recovery of intangibles (as defined in subsection (b)) had been used with respect to such costs.

(C) Net income from oil, gas, and geothermal properties.— For purposes of subparagraph (A), the amount of the net income of the taxpayer from oil, gas, and geothermal properties for the taxable year is the excess of—

(i) the aggregate amount of gross income (within the meaning of section 613(a)) from all oil, gas, and geothermal properties of the taxpayer received or accrued by the taxpayer during the taxable year, over

(ii) the amount of any deductions allocable to such properties reduced by the excess described in subparagraph (B) for such taxable year.

(D) Paragraph applied separately with respect to geothermal properties and oil and gas properties.—This paragraph shall be applied separately with respect to—

(i) all oil and gas properties which are not described in clause (ii), and

(ii) all properties which are geothermal deposits (as defined in section 613(e)(2)).

and of retaining some incentive for particular economic activities. The deduction of intangible drilling costs is treated as a "preference" because such expenses normally would be capitalized and amortized over the life of the mine. Under the government's theory of the purpose of the minimum tax, such amounts should be treated as preferences in full. However, Congress has chosen a more limited approach, treating these benefits as subject to the minimum tax only to the extent they exceed 65 percent of the taxpayer's net income from oil, gas and geothermal properties. Thus, Congress, in the "intangible drilling cost" preference, has sought to achieve a balance between the desirability of encouraging mineral development, on the one hand, and the desire to curtail tax benefits, on the other. Precisely the same kind of balance is involved here.

Nor is there anything inherently illogical about such an approach. The government itself concedes that Congress has long favored certain oil and gas and mineral producers. (Br. at 3.) As the court below noted, Congress, in the preference for percentage depletion as well as in the preference for intangible drilling costs, apparently wished to preserve some of the tax benefits under the minimum tax and thus to encourage mineral development. This case turns on the clear language of the statute, not on petitioner's perception of the "logic" underlying the minimum tax.

II. EVEN IF THE STATUTE WERE AMBIGUOUS, THE TREASURY'S OWN REGULATIONS INTERPRETING THE STATUTE ARE A REASONABLE INTERPRETATION AND ARE ENTITLED TO DEFERENCE.

Even if the statute were not plain on its face, the Treasury's own regulations make clear that the adjusted basis of a mineral deposit includes the tangible improvements to the property.

This Court has "long recognized that considerable weight should be accorded to an executive department's construction of a statutory scheme it is entrusted to administer. . . ." *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 844 (1984). The weight accorded administrative interpretations has, if anything, been especially great in the highly technical and specialized area of taxation.[16] A government agency, as much as a private party, is bound to follow the agency's administrative interpretations.[17]

And the regulations here are quite clear. Petitioner's specific regulations under Section 57 of the minimum tax provide: "For the determination of the adjusted basis of the property at the end of the taxable year *see section 1016 and the regulations thereunder.*" 26 C.F.R. § 1.57-1(h)(3) (emphasis added). This is the regulation that petitioner has issued specifically to define "adjusted basis of the property" for purposes of section 57(a)(8). It appears in a portion of the regulations devoted specifically to the minimum tax, which is the portion of the tax laws at issue in this case. It is the *only* regulation that petitioner has issued in order to define that term for purposes of section 57(a)(8). And this regulation sets forth the definition plainly and unequivocally. "Adjusted basis of the property," for purposes of section 57(a)(8), is adjusted as provided in section 1016 and the regulations thereunder.

[16] *See, e.g., Commissioner v. South Texas Lumber Co.*, 333 U.S. 496 (1948); *National Muffler Dealers Ass'n, Inc. v. United States*, 440 U.S. 472 (1979).

[17] *See Fort Stewart Schools v. Federal Labor Relations Authority*, 495 U.S. 641, 654 (1990) ("It is a familiar rule of administrative law that an agency must abide by its own regulations"); *Helvering v. R.J. Reynolds Tobacco Co.*, 306 U.S. 110 (1939) (applying this principle to an attempt by the Commissioner to disavow a tax regulation).

Petitioner's regulations under section 1016 provide:

> The cost or other basis shall be properly adjusted for any expenditure, receipt, loss, or other item, properly chargeable to capital account, *including the cost of improvements and betterments made to the property.*

26 C.F.R. § 1.1016-2(a) (emphasis added).[18]

Petitioner seeks to avoid the obvious consequences of its own regulations by suggesting that, in the case of mineral property, the regulations do not mean what they say. Petitioner's primary support for this view of its own regulations is that *another* section includes a special definition of "adjusted basis" that excludes tangible improvements.[19] As we have discussed earlier, and as the

[18] The language of today's 26 C.F.R. § 1.1016-2(a) apparently originated in the House Ways and Means Committee report accompanying the 1924 Revenue Act:

> [T]he cost or other basis of the property . . . shall be increased by the amount of items properly chargeable to capital account and decreased by depreciation and similar deductions allowed with respect to the property. Under this provision capital charges, *such as improvements and betterments* . . . are to be added to the cost of the property . . . .

H.R. Rep. No. 179, 68th Cong., 1st Sess. 1924), *reprinted in* 1939-1 (Part 2) C.B. 241, 250; see generally 2 Boris I. Bittker & Lawrence Lokken, *Federal Taxation of Income, Estates and Gifts* ¶ 42.1 at 42-2 (2d ed. 1990). This regulation has been in effect at least since 1932. *See* United States Dep't of the Treasury, *Regulations Relating to the Income Tax Under the Revenue Act of 1922*, art. 605 (1933). The longstanding nature of this interpretation entitles it to particular weight. *Pauley v. Bethenergy Mines, Inc.*, 111 S. Ct. 2524, 2535 (1991).

[19] Petitioner also seeks to find some support for its position in the fact that the depletion regulations, at one point, contain a definition of "mineral enterprise," which is distinguished from "mineral deposit." (Br. at 22.) The very limited use of the term "mineral enterprise" in petitioner's regulations has nothing whatever to do with this case. The term "mineral enterprise" is used five times in petitioner's tax regulations. The first time it appears, in 26 C.F.R. § 1.611-1(d)(3), the term is simply defined. It also appears in 26 C.F.R. § 1.611-1(d)(4), dealing with the apportion-

government concedes, (Br. at 18 n.13), the regulations under section 612 deal only with *cost* depletion. 26 C.F.R. § 1.612-1(b)(1). Petitioner did *not* create a special definition of this kind in section 1.57-1(h)(3), the one regulation governing the depletion preference under the minimum tax. Nor have the regulations under section 57 adopted the adjusted basis provisions in the section 612 regulations. Instead, petitioner has provided explicitly in that provision that the Code's regular definition, of 26 U.S.C. § 1016 and the regulations thereunder, shall apply.[20]

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ment of cost on the acquisition of a mineral interest; 26 C.F.R. § 1.611-2(e), dealing with the valuation of mineral properties by reefrence to the operating record of the mineral enterprise; 26 C.F.R. § 1.612-1(c), which is simply a cross-reference to the definitions of section 1.611-1(d)(3); and 26 C.F.R. § 1.613-4(i), dealing with extraction from waste or residue. It is difficult to see how the use of this phrase in these peripheral regulations detracts anything from the meaning of 26 C.F.R. § 1.57-1(h)(3), which petitioner promulgated precisely to address the statutory provision at issue in this case.

Petitioner also seeks to gain comfort from regulations that, for various purposes of tax accounting, require a taxpayer to maintain more than one cost recovery account for a single property. (*See* Br. at 22 and n:15, *citing* 26 C.F.R. §§ 1.611-2(b)(1), 1.611-5(c), and 1.167(a)-7.) For example, the different buildings in an apartment complex might have been constructed at different times, under different legal regimes, and be subject to depreciation at different rates. Similarly, as the current case demonstrates, some elements of a mineral property may be depletable, some may be depreciable, and some amortizable as deferred development expenses. The maintenance of these separate accounts within the same property does not derogate from the unity of the property, as 26 U.S.C. § 611(a), quoted at p. 11, illustrates.

[20] The very fact that under section 612 petitioner apparently perceived a need to specify that it was departing from the general rule, and to specify in section 1.612-1(b) that adjusted basis does *not* include depreciable amounts for purposes of cost depletion, suggests that in the absence of specification to the contrary, adjusted basis *does* include such amounts.

Petitioner in its brief not only ignores the relevant regulations[21] but also ignores Technical Advice Memorandum ("TAM") 8314011, a private ruling that petitioner issued in 1982 and which strongly supports the taxpayer's position. Tech. Adv. Mem. 8314011 (Dec. 22, 1982). TAM 8314011 involved the question whether certain "deferred development expenditures" should be included in a property's "adjusted basis" for purposes of the same minimum tax provision involved in this case. Like the costs of depreciable tangible improvements, deferred development expenditures are amortized not by depletion but by a separate capital recovery scheme. *See* 26 U.S.C. § 616. Indeed, deferred development expenditures generally include costs of depreciable tangible property used in developing a property.[22] Thus, deferred development expenses include the costs of tangible improvements, and are indistinguishable from the costs of tangible improvements involved here.

In TAM 8314011, the IRS determined, in language equally applicable to this case, that deferred development expenses should be included in "adjusted basis of the property" for purposes of section 57(a)(8). The IRS said:

> The term "adjusted basis" has the same meaning whether used in section 57(a)(8), section 612, or elsewhere in the Code except where the term is specifically defined differently. Section 1.57-1(h)(3) of the regulations dealing with the definition of adjusted basis uses section 1016 and the regulations thereunder. *There is no separate authority for determin-*

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[21] It is noteworthy that petitioner's brief cites a great many tax regulations, (Br. at v-vi), but does not once cite 26 C.F.R. § 1.57-1(h)(3), the regulation that is most directly applicable to the question in this case.

[22] *See* 26 U.S.C. § 616(a) (final sentence); 26 C.F.R. § 1.616-1(b)(2). The costs added to basis under this provision are limited to the amounts attributable to depreciation during the development period.

> *ing an "adjusted basis" for purposes of the minimum tax, and another for determining gain or loss on the sales of property.*

(Emphasis added.) *Cf. Patterson v. Shumate*, 112 S. Ct. 2242 (1992). Such TAMs are entitled to consideration by the courts under *Chevron*, even though by statute they are not conclusive on the agency.[23] The approach taken in the TAM is completely inconsistent with the government's litigation position in this case.

Petitioner's regulation (section 1.57-1(h)(3)) and its technical advice memorandum plainly demonstrate acceptance of the principle that the adjusted basis of a property includes the unrecovered cost of improvements to the property. It is only today, long after the promulgation of 26 C.F.R. § 1.57-1(h)(3) and TAM 8314011, that petitioner seeks to apply a special definition of adjusted basis. Petitioner should not now be permitted to disavow this interpretation.

In the past this Court has repeatedly declined to permit the government to reject its previous interpretation of the tax laws. In *Hanover Bank v. Commissioner*, 369 U.S. 672 (1962), the Commissioner suddenly found fault with a longstanding administrative interpretation that permitted bondholders to assume, for purposes of amortizing and deducting premiums paid on the acquisition of bonds, that the bonds would be redeemed at the "special call price," which typically is lower than the price at which bonds actually are redeemed. The Commissioner's interpretation thus allowed taxpayers to claim deductions that were, quite clearly, greater than required to compensate them for their economic costs, but the Commissioner belatedly sought to repudiate the prior administrative position. This Court rejected the Commissioner's attempt because "[t]he regulations in effect [as of the tax year at issue] give no support to the Government's present contention" and because the government had previously rejected it. 369 U.S. at 686-87. Here, as in *Hanover Bank*, petitioner's regulations give no hint of the position that petitioner now asserts, and the Treasury should not be permitted to disavow its earlier view.

[23] *Hanover Bank v. Commissioner*, 369 U.S. 672, 686 (1962) (Court states that private rulings, while not constituting formal precent, "reveal the interpretaiton put upon the statute by the agency charged with the responsibility of administering the revenue laws"); *accord, Rowan Cos., Inc. v. United States*, 452 U.S. 247, 261 n.17 (1981).

Petitioner cannot, of course, claim that its litigation position put forth in this case is, in itself, an "interpretation" entitled to deference. This Court has explicitly rejected deference to such ad hoc "interpretations." *See Bowen v. Georgetown University Hospital*, 488 U.S. 204, 212 (1988); *Cottage Savings Ass'n v. Commissioner*, 111 S.Ct. 1503, 1509 (1991). In *Bowen*, the Secretary of Health and Human Services abandoned a past interpretation of a Medicare reimbursement provision, offering a different interpretation for the first time in his appellate brief. 488 U.S. at 212-13. This Court refused to pay "[d]eference to what appears to be nothing more than an agency's litigating position," noting that the Court had "never applied the [*Chevron*] principle . . . to agency litigating positions that are wholly unsupported by regulations, rulings or administrative practice." 488 U.S. at 213, 212. *See also Cottage Savings Ass'n v. Commissioner*, 111 S.Ct. at 1509 (deference is warranted only to "an authoritative, prelitigation interpretation").

CONCLUSION

For the foregoing reasons the decision of the Court of Appeals should be affirmed.

Respectfully submitted,

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